

*Targeted Community Reinvestment:  
HUD's Section 108 Loan Guarantee Program as a Financing Tool*

# Program Design & Application Process Part 1 of 2

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# Panelists

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# Webinar Topics

- Program Overview
- Program Considerations
- **Individual Project** Application Process
- Case Study—City of Cleveland
- **Loan Fund** Application Process
- Case Study—State of Iowa
- Wrap Up and Next Steps



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# Program Overview

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# About the Section 108 Program...

- Provides *loan guarantees*, not grants
- Employs the framework of the Community Development Block Grant (CDBG) Program
- Offers recipients (states, cities and counties, and insular areas) a means of accessing low-cost financing from capital markets



# About the Section 108 Program...

- Non-competitive
- Rolling application process
- Not a general obligation
- Maximizes impact of available grant funds (up to 5x most recent CDBG grant amount)



# About the Section 108 Program...

The program enables HUD to guarantee loans issued by recipients for three basic types of development:

- Economic Development
- Public Facilities
- Housing Rehabilitation



For More Information on Eligible Activities,  
see 24 CFR 570.703.





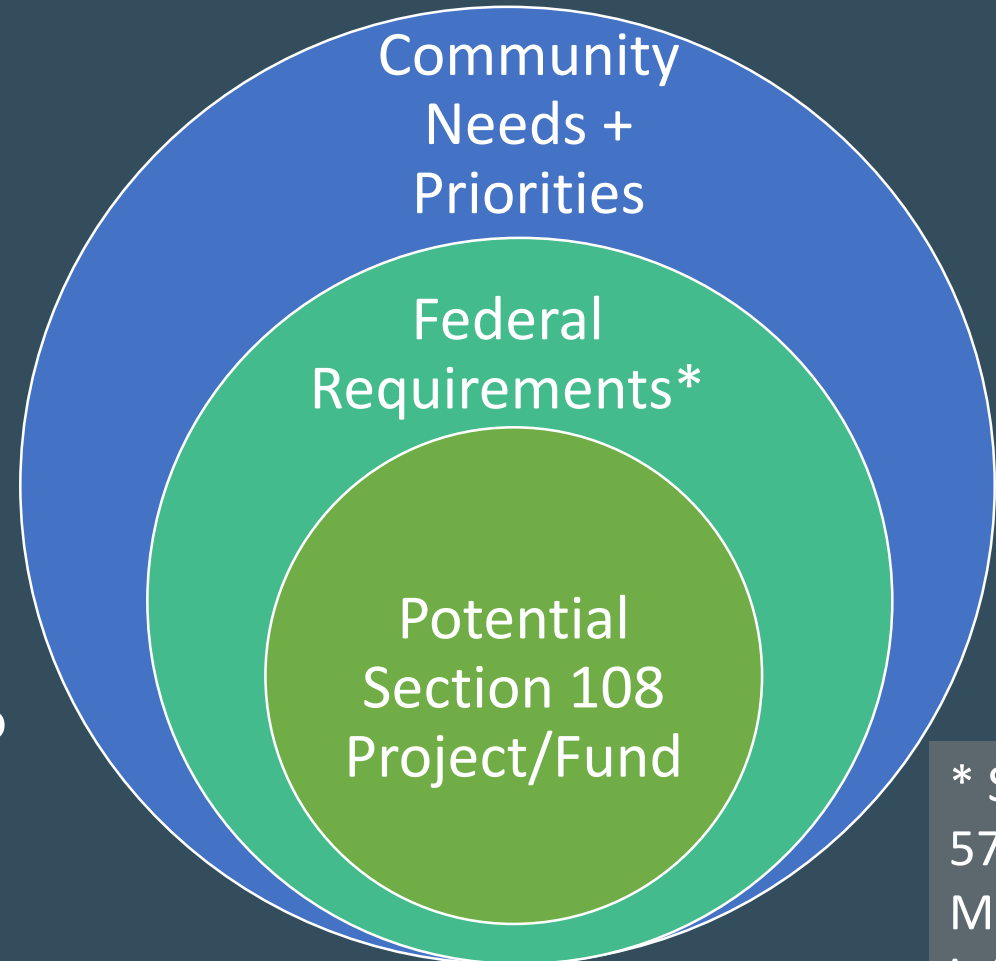
# Program Considerations



# Keep in Mind “The Big Picture”

## Before you apply, ask yourself:

- Does using Section 108 guaranteed financing make sense for this program/project?
- Do we or our partners have the capacity, experience, and tools (loan processing/underwriting) in place to administer the program successfully?



\* See 24 CFR 570, Subpart M for more information

# Keep in Mind “The Big Picture”

- Does the project create sufficient revenue to pay debt service, preserving CDBG funds for other projects or programs? Or, are there other sources that will be used to repay the loan (e.g. Tax Increment Financing)?
- Has the community reviewed regulatory pre-submission, citizen participation, and certification requirements? [See CFR 570.704 (a) & (b)]

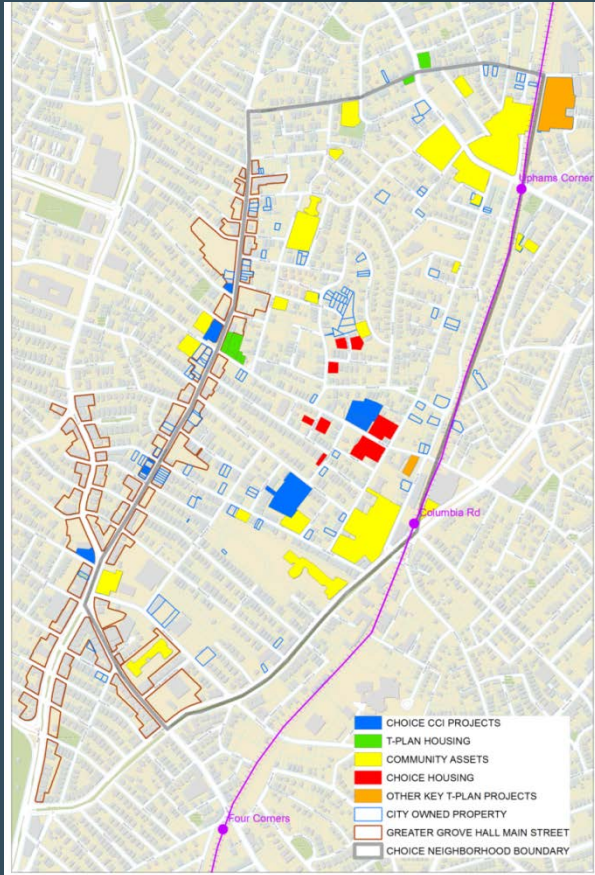


# What to consider before using Section 108

1. Community Strategy—*What are the community's needs?*
2. Organizational Arrangements—*Who is responsible?*
3. Program Design—*At what scale?*
  - *Individual Project*
  - *Loan Fund*



# Community Strategy



- What do local comprehensive plans identify as needs, goals and strategies?
- What economic and community development needs and challenges will your community be addressing?
- What's already in play?

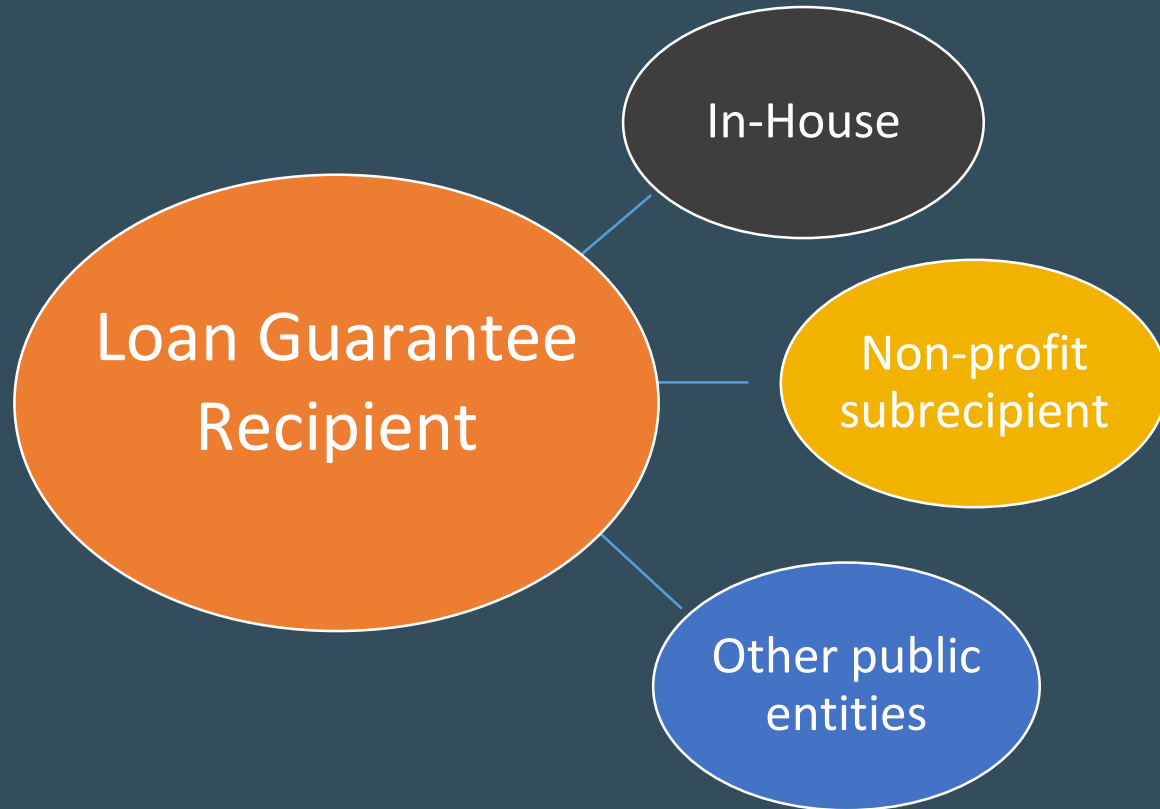
# Community Strategy



- Is the Section 108 Program a good match for community needs?
- What is the community's capacity and experience with lending programs?
- Does the willingness exist to pledge its CDBG funds in case of nonpayment?

# Organizational Arrangements

What entity will manage or operate the program?



Internal staff, directly administered by recipient

Subrecipients—e.g. Community Development Corporations and CDFI's

Other public entities on behalf of recipient—e.g. Economic Development Authority or Redevelopment Authority

# Individual Project



- Approach used by majority of borrowers
- Application is for a specific project
- Application requires detail and specificity
- After HUD approval, guaranteed loan would be used by the recipient or re-lent to a 3<sup>rd</sup> party borrower

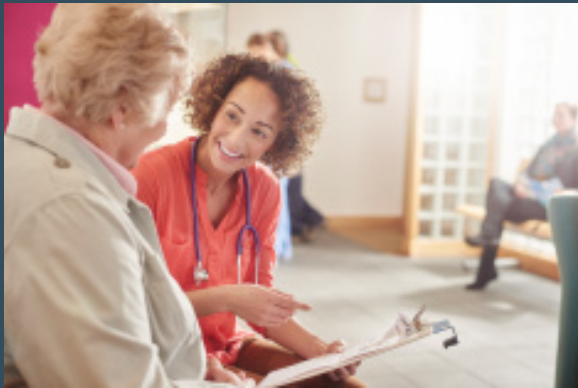


# Individual Project

## Example project-specific loans:



- Renovation of an unused industrial space into a mixed-use facility with office, medical, and arts space
- Redevelopment of a former department store into a business incubator
- Conversion of a former historic school building into affordable rental housing
- Acquisition of a site for future senior housing including a health care clinic
- Remediation and redevelopment of an old industrial site into an employee-owned cooperative greenhouse
- Conversion of former power plant into education and recreational site, for sailing, adventure sports, museum, and amenities





# Loan Fund



- Application contains program description and program requirements for activities that meet community goals
- Individual transactions do not have to be identified within the application, but HUD's preference is for a pipeline of projects to be identified
- Prior to providing loan guarantees to an individual project under the fund, HUD must first make a determination of program compliance



# Loan Fund

## Example Loan Fund objectives:

- Promote local strategies such as transit oriented development or mixed-use development
- Assist businesses located in blighted areas to provide job opportunities to residents and provide key services
- Fund acquisition activities for non-profit developers to develop affordable housing
- Provide “gap financing” to for-profit and non-profit developers who develop in community target areas (such as promise zones, main streets, or specific neighborhoods)
- Encourage new grocery stores and other healthy food retail development in local ‘food deserts’





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# Individual Project – Application Process

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# Individual Project Application Process

- ✓ Step 1: Evaluate potential project in terms of community strategy
- ✓ Step 2: Determine whether proposed use of funds is eligible under the program
- ✓ Step 3: Underwrite project(s) for financial feasibility
- ✓ Step 4: Complete citizen participation process and local review
- ✓ Step 5: Application Submission and HUD Approval
- ✓ Step 6: Issuance of the loan guarantee



# STEP 1: *Evaluate Potential Projects In Terms Of Community Strategy*



Aging  
infrastructure



Need for workforce  
housing



Employment opportunities  
for vulnerable populations



Rehabilitation of  
blighted properties



Unmet needs of local small businesses

## ***STEP 2: Determine Whether The Proposed Use Of Funds Is Eligible***

- Is the proposed use of the guaranteed financing an eligible activity?
- Does it meet a CDBG National Objective?
- Will it contribute to the requirement that 70% of all CDBG/108 expenditures benefit low/mod persons?
- If applicable, does it meet public benefit standards?



## ***STEP 2: Determine Whether The Proposed Use Of Funds Is Eligible***

It is essential that you consider cross-cutting regulations, such as:

- What type of environmental review do I need to undertake?
- If applicable, who will ensure compliance with Davis Bacon?
- Will the project result in the displacement of any tenants or businesses?
- If applicable, how will the use of funds affirmatively further fair housing?



## ***STEP 3: Underwrite Project(s) For Financial Feasibility***

- Is the project ready to go? (e.g. site control, zoning approval)
- Does the project meet a market demand?
- Is there adequate committed financing from all sources?
- If this is a 3<sup>rd</sup> party loan, can the borrower fulfill the terms of the loan?
- Is there sufficient loan collateral for the proposed Section 108 financing?





# STEP 3: *Underwrite Project(s) For Financial Feasibility*

## Real Estate Loans

Section 108 Underwriting Guidelines  
for Income-Producing Projects



## Business Loans

Section 108 Underwriting Guidelines  
for Business Credit Loans



HUD has created guidelines for evaluating and selecting economic development projects found at 24 CFR 570.209 - Appendix A

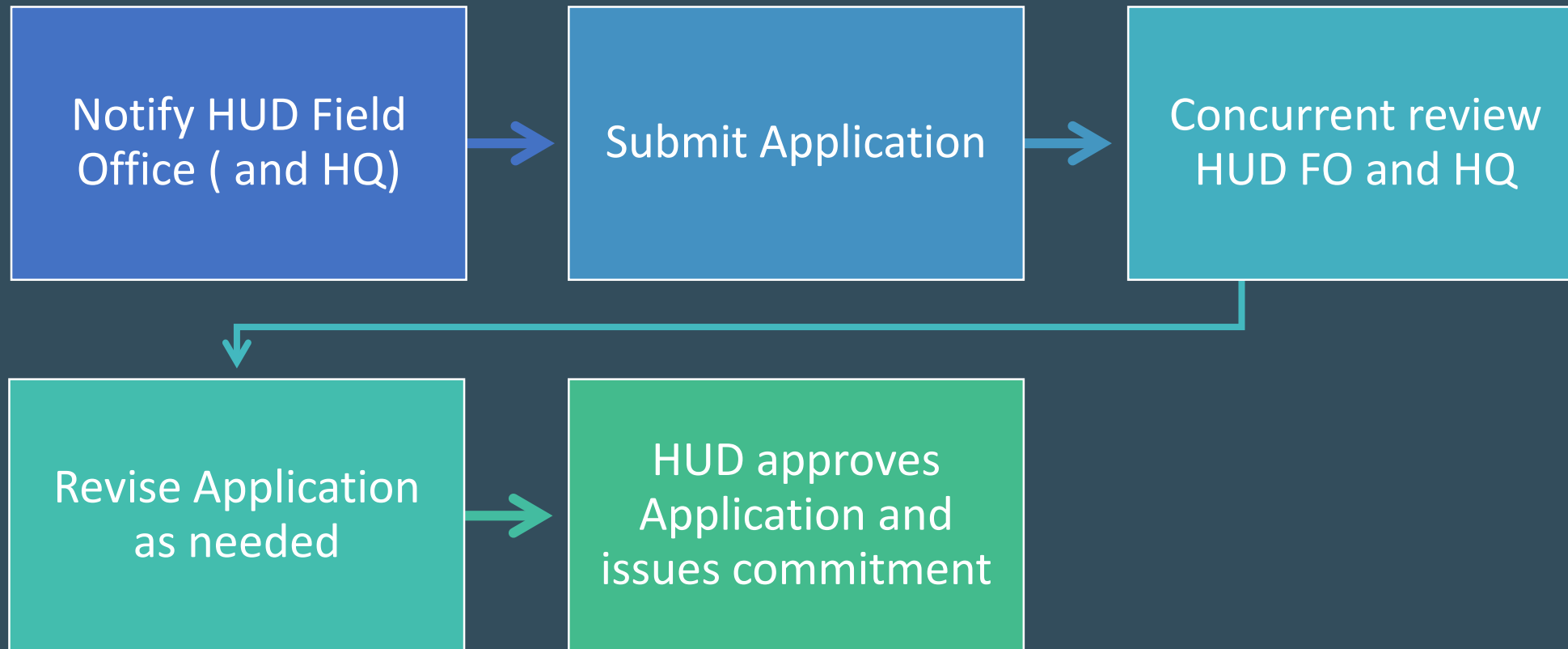


# **STEP 4: *Complete Citizen Participation And Local Approval***

- Follow your HUD Citizen Participation Plan
- Solicit input from local stakeholders
- Advertise availability of draft application
  - Newspaper, flyers in the community/newsletters, existing email lists
- Make application available electronically as well as via hard copy (e.g. public libraries)



# STEP 5: *Application Submission & HUD Approval*



# Individual Project Application Contents

- Proposed community development objectives
- Project Description, including:
  - Organizational Arrangements/Key Participants
  - Project Timeline/Development Phases
- Project Financial Information
- Repayment Schedule
- Pledge of CDBG Funding
- Description of Additional Collateral
- One Year Action Plan Amendment/Citizen Participation Comments
- Certifications



*[See full list of requirements at 24 CFR 570.704]*



# Project Description

- Typically in narrative form and accompanied by supporting documentation such as:
  - Market or feasibility studies, renderings, underwriting reports, etc.
- Must include :
  - Description of activities to be financed
  - Eligible activity or activities (include citation)
  - National objective(s) to be met (include citation)
  - If applicable, how project meets public benefit standard



# Organizational Arrangements

Who will be the key participants carrying out the proposed activities/development project?

- Users of loan guarantee financing
  - Recipient/Borrower
  - Developer
  - Business



# Project Timeline/Development Phases

- Expected closing date of Section 108 financing
- Expected closing date with 3<sup>rd</sup> party borrowers
- Development phases, if applicable
- Estimated start date (when project expected to become operational—lease-up date, etc.)



# Financial Information

- Sources and uses
  - including sources of construction financing and permanent financing
- Estimated revenue and expenses
- Debt service analysis
- Proposed repayment schedule
- Additional collateral for the Section 108 guaranteed financing
- Financial information for key project partners
  - (e.g. developer or 3<sup>rd</sup> party borrower)
- Payment information for HUD's Loan Guarantee Financing Fee





# Sources

- Commercial Loans
- Owner Equity
- Tax credit equity—New Market, Low-Income Housing, or Historic
- CDBG funds
- Other public/private sources



# Uses

- Site Acquisition
- Marketing Costs
- Pre-development costs (site prep, etc.)
- Construction
- Professional fees
- Finance Costs
- Relocation
- Reserves
- Business Expansion—machinery, equipment, operating capital, inventory



# Loan Guarantee Financing Fee

- Charged starting with FY 2016 commitments
- One time, upfront cost (not annual)
- Not added into the interest rate of the loan
- The fee can be financed as part of the guaranteed loan amount, paid for with CDBG funds or with another source of funding.
- FY 2016 Fee is 2.58% of the Principal Amount of the loan disbursed for eligible use(s)

*For more info see “Announcement of Fee to Cover Credit Subsidy Costs”  
in the 11/03/15 Federal Register*



# Repayment Information

- Source of repayment
  - Cash Flow from a Business
  - Net Operating Income from Real Estate
- Annual principal repayment schedule
- Loan term can be up to 20 years



# Collateral

- In addition to the required pledge of CDBG funds, collateral for Section 108 financing must be described
- Most loans are secured by a combination of additional collateral, including:
  - Liens on real property, machinery, equipment, inventory and accounts receivable
  - Revenue from other sources, including parking, special taxing districts, or loan portfolios
  - Personal guarantees from 3<sup>rd</sup> party borrower



# Certifications & CDBG Pledge

Refer to 24 CFR 570.704(b)(3)-(9), including but not limited to:

- Citizen participation
- Pledge of CDBG funds
- Legal authority to submit application
- Governmental resolution to authorize an official to execute loan documents
- Provision of assurance that public entity has made efforts to obtain alternate financing



# STEP 6: *Issuance Of The Loan Guarantee*

- HUD approves the application and issues an offer of commitment
- The Recipient (borrower) requests the advance of funds through IDIS
- HUD sends a Contract Documents for Legal Review
- The borrower's counsel issues a legal opinion
- The borrower returns the legal opinion, executed promissory note, and contract with related documents to HUD and HUD performs due diligence on the documents
- Following review, HUD executes the federal guarantee for the borrower's promissory note

